Petition

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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1981

No. _____

PHILIP GUTTER
Petitioner
Pro Se

MERRILL, LYNCH, PIERCE, FENNER, & SMITH, INC.
Respondent

PETITION FOR WRIT OF CERTIORARI

To the United States Court of Appeals

For the Sixth Circuit

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QUESTIONS PRESENTED

Whether a person who brings a "suit in equity and an action at law brought to enforce a liability or duty created" by the 1934 Securities Exchange Act section 27 can be denied a private cause of action against his broker for a violation of section 7 of the Act and Regulation T promulgated thereunder by the Federal Reserve Board?

Whether this Court's four-pronged condition respecting an implied cause of act-

ion for a violation of a Federal statute as it indicated in the CORT-ASH case (422 U.S. 66)(1975) involving section 610 of the Federal Elections Law and now being used in cases involving violations of federal securities laws, is now "moot" since the section 610, supra, has been repealed by Act of May 11, 1976; P.L. 94-283, TitleII para. 201 (a), 90 Stat. 496?

Does not a person have a private cause of action against his broker under Section 29 (b) of the 1934 Act, be it implied or explicit, to void contracts of transactions in securities which were made "in violation of any provision of this title or of any rule or regulation thereunder"?

Since this Court has stated that "short selling" falls within the provisions of 17 (a) of the 1933 Act(U. S. v. NAFTALIN, 39 CCH S. CT. BULL.,p B2618), is it not so that the 6th Circuit Court was in error in holding that only "purchasers" have recourse to 17(a) and its provisions?

This Court in its holding in CASE v. BORAK (377 U.S.426) states on pages 430, 431:

> " It appears clear that private parties have a right under #27 to bring suit for violation of 14(a) of the Act. Indeed, this section specifically grants the appropriate District Courts jurisdiction over 'all suits in equity and actions at law brought to enforce any liability or duty created' under the Act."

Thus, was not the 6th Circuit Court in error in its denial to the Petitioner of a private right of action against the Respondent?

Did not the Petitioner also have a private right of action against the Respondent for violations of section 17(a) under section 22 of the 1933 Act?

Does not the Petitioner have a private right of action under 29(b) of the 1934 Act to void a purchase or sale transaction for a margin rule violation section 7 and Regulation T promulgated thereunder by the Federal Reserve Board.(12 C.F.R. 220.1 ff)

May not a plaintiff void a stipulation made by his counsel (previous counsel) that dismissed a claim of a margin violation under Regulation T and Section 7 of the 1934 Act because the transactions involved, the writing or sale of uncovered options, took place prior to January 1, 1977? The previous counsel was unfamiliar with the fact that since the enactment of the 1934 Act Regulation T always contained an initial margin requirement for the broker to receive from his customer for the broker's guarantee of the uncovered option sold.

Given that the Federal Reserve Board made changes in Regulations T and U effective as of March 11, 1968 by the addition of a Special Bond Account to Regulation T and by making the margin required a good faith one, that is by making the maximum loan values of non-equity securities good faith loan values and restricting transactions in non-equity securities (bonds) to the Special Bond Account after March 11, 1968, is it not

so, that, as a matter of law, a transfer of the maximum loan values of non-equity securities from the Special Bond Account to the General Account to furnish initial margin requirements for transactions in the General Account violates Regulation T because of the fact that maximum loan values of non-equity securities are so much higher than maximum loan values of securities lying in the General Account, thus causing "excessive credit" to enter the markets, to prevent which the 1934 Act was enacted? With respect to this question this Court is reminded that transactions in the General Account are regulated under Regulation T as to maximum loan values while maximum loan values involved in non-equity securities are unregulated values, that is, not regulated by the Federal Reserve Board, but are "good faith" loan values controlled by the creditor solely.

Given that a district court in its interlocutory judgment has found that the respondent here has violated Regulation T and that the Petitioner here was entitled to be

awarded damages for his losses sustained in his General Account, is it not reversible error for the district court in its charge to the jury in this litigation under a common law claim and a claim under Section 10 of the 1934 Act and rule 240.10(b)(5) promulgated thereunder not to indicate to the jury that it had already awarded damages to the then Plaintiff as a result of the then Defendant's violation of Regulation T? The district court's jury charge is found on page 150 of the Appendix furnished the 6th Circuit Court.

Given Section 7(f) of the 1934 Act and the Federal Reserve Board's Regulation X promulgated thereunder and given that the 6th Circuit Court relied on these to deny the Petitioner a private right of action and given differences of opinion of the courts in their interpretations of 7(f) and Regulation X and given that there are 1,250,000 margin customers of brokers, all being borrowers, and thus all being potentially ad-

versely affected by potentially wrongful interpretations, the Petitioner respectfully requests this Court to interpret once and for all that a customer of a domestic broker in the making of a transaction in our domestic securities markets on credit, that is, on margin, does in no way fall within the ambit of 7(f) or Regulation X, since Congress enacted enacted 7(f) and the Federal Reserve Board enacted Regulation X for the purpose of preventing the use of credit obtained from a foreign lender since that credit could not be regulated by the Federal Reserve Board which regulates credit in our domestic securities markets, through Regulations T, U, and G.

Given 220.4(a)(2) of Regulation T which states:

> Each such special account shall be recorded separately and shall be confined to the transactions and relations specifically authorized for such account by the appropriate paragraph of this section and to transactions and relations incidental to those specifically authorized. An adequate record shall be maintained showing for each such account the full details of all transactions in the account.

The question here becomes: Is it not so that since the Special Bond Account is one that is "recorded separately" and is "confined to the transactions and relations specifically authorized for such account by the appropriate paragraph of this section"(220.4(i)), this section allowing only for the "effecting and financing of nonequity and exempt securities" a broker is in violation of 220. 4(a)(2) and thus is subject to a suit under Section 27 of the 1934 Act to "enforce any liability or duty created by this title or rules and regulations thereunder" and is probably also in violation of Section 10(b) of the 1934 Act and the concomitant 240.10 (b)(5) rule promulgated thereunder? The complaint in this case stated, inter alia, both of these charges.

Another question presented to the Court: Given that MANEVICH v DUPONT (338 F. Supp. 1124) has legitimized the use of the Special Miscellaneous Account as a source of buying power for initial margin in credit tra-

nsactions in the general account; given that "the adjusted debit balance" computation of Regulation T (220.3(d)) is the duty of the broker; given that the creditor (broker) is charged the account keeping of his customer; given that a customer has no way of knowing the status of his account except thru his monthly statement or thru an oral unproven statement by his broker's representative to be accepted "in good faith", then it follows as night follows day that 7(f) and Regulation X, in saying that a "borrower" in obtaining credit shall "conform to the provisions of Part 220 of this chapter (Regulation T) and seemingly placing a liability of being "unlawful" on the "borrower" when it is an impossibility for the "borrower" to know the status of his account under the continuous changing of market values that take place in our marketplace, is saying something that this Court, in the opinion of the Petitioner, should be not averse to declaring unconstitutional, as now written. This is so because the intent of Congress in enacting 7(f) was to prevent an American investor from obtaining credit

from a foreign lender whose credit for securities transactions is not regulated by the Federal Reserve Board. Domestic brokers' credit is regulated by the Board.

Since many courts have concluded that section 7 relates to macroeconomic conditions and not to the "protection of investors" and thus make for their denial of an implied private right of action; then, does this Court not agree that an analysis of section 7 at (d)(E) stating:

> (E) to such other loans as the Board of Governors of the Federal Reserve System shall by such rules and regulations as it may deem necessary or appropriate in the public interest or for the protection of investors, exempt , -----.

indicates that Congress intended that the Board's rules and regulations were for the "protection of investors"? The Petitioner believes that this is the first instance of this Court being asked to interpret this macroeconomic versus "protection of investors" intention of Congress.

Given, that all of the transactions detailed in this case: 2 long purchases, 11 short sales and 5 uncovered options were effected in the general (margin) account; given that that the deposit of bonds requested by Merrill, Lynch to be used as collateral for uncovered option writing in the general account and as subsequently used for initial margins for 11 stock short sales and 2 stock purchases and were illegal uses for purposes of collateral in general accounts as the district court has so stated in its 9-9-1977 opinion and order, is it not so that this is a clear violation of 17(a) of the 1933 Act and also at the same time a violation of section 10 of the 1934 Act and the 10(b)(5) section promulgated thereunder?

Given that the Petitioner is in possession of a Merrill, Lynch letter stating that it is too time consuming and expensive to send to the Petitioner a copy of the Special Miscellaneous Account (the "borrowing power account" and of crucial importance to

a proper understanding of this case) in August of 1975,(before this case was instituted) and given that Merrill, Lynch's monthly statement stated that this account would be sent upon request; and given that M-L in fact entered an affidavit and exhibit in the record, stating, inter alia, that it maintained this account "in the ordinary course of business",(page 37 of the Appendix used in the 6th Circuit below) depriving the Petitioner of the mathematical proof of the fraud it was perpetrating upon him, then, is it not so M-L is in violation of 10(b)(5)?

Given in the Petitioner's amended complaint, that the combining of losses to be voided in Count 1 with the losses detailed in Count II by reference in Count II, all having taken place in the general account, are losses which have the same operative facts, that is, violations of Regulation T of the Federal Reserve Board, given that the same operative facts are violation of margin requirements and given that these losses can not be separated from each other, that is,

in reality, none of the transactions involving losses should have been effected by M-L in the first place because of the "no loan value" status of non-equity securities in the general account, given that the district court has ruled that the Petitioner was to be awarded damages as to the losses detailed in Count II, given that Count II included by reference losses of Count I, given that the district court accepted a stipulation that inferred no margin requirement was involved in the writing of uncovered options when the opposite was true (Appendix p. 71 of the 6th circuit), given that the district court accepted and conducted a 3 day trial presumably for the purposes of awarding or not awarding damages, then the question before this Court is: was the district court in error in conducting the jury trial and in charging the jury with an extremely complex charge without telling the jury that the court had already found M-L guilty of violating section 7 of the 1934 Act and had held in a summary

judgment that the Petitioner was to be awarded damages. The Petitioner believes as a non lawyer that he was denied due process; had the jury been told of these events it is a certainty that it would have found in favor of the Petitioner, and in all fairness believes that this part of this case should be remanded to the district court which should be instructed to clarify its opinion and order so as to include in its award of damages the Petitioner's losses due to all transactions that took place in the general or margin account, losses due to short sales, long purchases and option writing as detailed in his amended complaint.

Given- an award of damages based on transactions taking place in a Petitioner's general account; given- the opening of the transaction in which the confirm notice shows the price paid, the commission paid, the taxes paid if any and the net total; given- the closing transaction in which the confirm notice shows the same factors and its net total given- that each transaction to be complete

must compose of an original long purchase and a subsequent sale or an original short sale and a subsequent repurchase of the borrowed security to return to the lender in order to net out the failure or success of the transaction; given- that an option writing loss is that of the difference between the closing transaction cost of buying back the option and the income received from its original sale, commissions included both ways; given- that the Regulation T margin requirement is based on either the net proceeds of a short sale or the net costs of a long purchase; then is it not so that the district court, in basing the calculation of the award on the non-inclusion of the commissions involved committed a reversible error to the Petitioner by not considering that commissions are as much a cost of a security transaction as the security cost itself and this is true of both the buy and sell side. The Petitioner requests this Court to indicate to the district court that this error is to be corrected on remand.

A critical and important question: Given 7(f) and its words:

"It is unlawful for any U.S. person --- to obtain---- the beneficial use of a loan-- from any lender for the purpose of purchasing or carrying U.S. securities if under this section or rules or regulations prescribed thereunder the loan or other credit transaction is prohibited or would be prohibited if it had been made--- (emphasis added)

given: an order to a broker for a margin transaction; given: the time to effect the transaction being measured in seconds or minutes; given: the broker retaining in street name possession of the purchased securities to be hypothecated as the collateral for the loan to be borrowed; given: the loan making the purchaser a borrower under 7(f); given: 7(f) stating the credit transaction must be one that is "prohibited or would be prohibited if it is made"; given: no transaction in the general or margin account under section 220.3 is "prohibited" at the time of the effecting of the transaction by the broker at which time the borrower will be sent a confirmation notice of the details of the transaction; then, is it not so that since 7(f)

makes the position of the borrower "unlawful" if he places an ordinary purchase order with his broker who is not "prohibited"in any way from effecting the transaction under Regulation T, thus 7(f) is placing a burden on the borrower impossible to perform if his credit transaction is effected by a domestic broker in whom the borrower must have a good faith belief that in the effecting of the transaction provisions of Regulation T will be followed by his broker and so it seems that it is incumbent on this Court to hold that 7(f) is a nullity as regards the borrower in a domestic transaction, that to apply a state of "unlawfulness" to a borrower for something he has no control over must be construed as being unconstitutional? The 6th Circuit below denied the Petitioner a private right of action wrongly by misinterpreting 7(f) thus giving this Court a nother reason for the granting ofthe Certiorari writ to the Petitioner.

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APPENDIX
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Note- The Sixth Circuit Court's opinion which is the subject of this Petition is located following page A9 of the Appendix.

CITATIONS

J.I. CASE v BORAK, 377 U.S. 426; page Q3

MANEVICH v DUPONT, 338 F. Supp.1124
page Q8

THE RISE AND FALL OF THE PRIVATE CAUSE OF ACTION FOR VIOLATION OF MARGIN REQUIREMENTS---Keith J. Kanouse, BankingLaw Journal, Vol. 98, No. 2, February 1981 page 133 ---------- page 4

All of the cited cases in the Amici of the Federal Reserve Board and the Securities and Exchange Commission in the Fourth Circuit case of SAMUEL STERN v. MERRILL, LYNCH, case no. 98-1377; and the amicus of the Securities and Exchange Commission in the case of SCHY v. FEDERAL DEPOSIT INSURANCE CORPORATION, no. 77-7581 in the Second Circuit; lodged with this petition --------- page 16

Lodged herewith "INFORMATION FOR INVESTORS" from the Securities and Exchange Commission -- titled "WHAT IS BUYING POWER" ---------- page 16

IN THE SUPREME COURT OF THE

UNITED STATES

October Term 198

No.

PHILIP GUTTER
Petitioner, Pro Se, Not a lawyer
2653 Floribunda Dr., Columbus, Ohio

v.

MERRILL, LYNCH, PIERCE, FENNER, & SMITH INC.
Respondent

PETITION FOR WRIT OF CERTIORARI

To the Court of Appeals for the Sixth Circuit.

The Petitioner, Philip Gutter, respectfully prays that a Writ of Certiorari be issued to review the judgment and opinion of the United States Sixth Circuit of Appeals entered in this case on April 3, 1981. A motion for a "rehearing in banc" was filed and denied on May 15, 1981. A request was filed in this Court for an extension of filing time for this writ which was granted by Justice White to September 14, 1981. A further extension was granted to October 12,1981.

JURISDICTION

The opinion of the 6th Circuit Court was entered on April 3, 1981. Petitioner filed with that Court a "Suggestion of a Party for Hearing or Rehearing in Banc" which was denied on May 15, 1981. The Petitioner received an extension of time to file this Petition to September 14, 1981 by Justice White. A further extension of time to file was granted by Justice White to October 12, 1981.

The jurisdiction of this Court is invoked under Supreme Court rule 17(a) and (c), also under 28 U.S.C.S. paragraphs 1254(1) and 2101(c).

STATUTORY PROVISIONS INVOLVED

The Statutes involved are:

Section 17(a) of the 1933 Securities Act
" 22 " " " " "
" 7 " " " Sec. Exch. "
" 10 " " " " "
" 27 " " " " "
" 29(b) " " " " "
Regulation T of the Federal Reserve Board and Regulation X

STATEMENT OF THE CASE

Merrill, Lynch, thru its employee Mr. Richard Cochran, induced Petitioner to sell uncovered options in August of 1974; the inducement resulting from the fact that no money in cash was required but a deposit of previously purchased fully paid for bonds was necessary. Subsequently, transactions were made in the General or Margin account on the basis of phone conversations with Mr. Cochran in which he orally quoted Petitioner's SMA (Special Miscellaneous Account; an account which denotes buying power; the credit balance residing in the general or margin account only). Every transaction made that is the subject of this case was a free one, that is, Merrill, Lynch had stated that the Petitioner had sufficient funds in his gen-

eral account to make the credit transactions made. The Petitioner received monthly statements and noticed that certain entries made showed transfers of money amounts that could not be mathematically reconciled on the statement. These transfers were from the Speial Bond Account to the general margin account. In questioning Mr. Cochran as to the meaning of these transfers, he stated that they were computer processed and obviously correct. The above discussed transactions ended in heavy losses to the Petitioner. As a result of the Petitioner not being able to reconcile the transfers shown on the monthly statement, he decided to visit the local law libraries to study and research the securities laws discovering that Merrill,Lynch had violated the securities laws and in so doing had perpetrated a fraud. Petitioner then instituted this suit.

The district court in an interlocutory judgment held that the Respondent had violated Regulation T and that the Petitioner was

to be awarded damages based on the court's opinion as to the method to be used to calculate the amount of damages. A number of variously calculated damages were stipulated and the district court in its final judgment accepted one of the number stipulated. The Petitioner then filed an appeal to the 6th Circuit Court of Appeals to contest the fact that the stipulated damage amount the district court used contained arithmetic errors and the court had, in deciding the method of the damage calculation, violated Regulation T provisions.

REASONS FOR GRANTING THE WRIT

The decision below involves a substantial federal question which concerns the lives and fortunes of 1,320,000 margin customers of brokerage houses. Practically all of the questions being presented to this Court have heretofore not been decided by this Court.

The Petitioner requests this Court to note in the Banking Law Journal (Vol.98,#2 February 1981), the statement of the commentator regarding implied private rights of action:

> "However, prudent lenders must be wary, because the Supreme Court has yet to make a holding that decides the issue once and for all and borrower's counsel have not yet given up the fight."(page 133)

and he continues on page 140:

"While the Supreme Court has yet to rule on whether an implied cause of action exists for violations of margin requirements, the Court has had an opportunity to determine whether an implied cause of action is created under other provisions of the Securities Exchange Act and rules promulgated thereunder."

The Banking Law Journal article continues In its conclusion:

"The exact state of the existance of an implied private cause of action for margin violations is unsettled and, unfortunately,depends upon the jurisdiction in which the action is brought. It would appear that the emer-

ging majority is firmly in favor of denying such a right to a private investor. This view can be buttressed by the fact that the Supreme Court and circuit courts of appeals in other areas of federal regulation have applied the CORT test and have concluded that an implied cause of action does not exist. However, plaintiff's counsel have been intermittently successful in carving out exceptions to the general rule. Hopefully, one day the Supreme Court will resolve the question once and for all."

The Petitioner, Pro Se, and having spent thousands of hours in law research on this case, could not state his justification for the granting of a certiorari writ more persuasively than the above commentator has in the context of a private cause of action for violations of margin regulations under Regulation T but as this Court will see from the questions presented to it, the the court below did not consider the effect of 29(b) and of section 27 of the 1934 Act on private rights of action, this Court having indicated in its BORAK holding that a private right of action exists under section 27 of the 1934 Act. Thus, the court below did decide a federal question in a way in conflict with applicable decisions of this Court and so falls within the ambit of this Court's rule 17.(Considerations Govern-

ing Review on Certiorari).

The district and circuit courts disagree as to the effect of 7(f) and Regulation X on the private right of action implication to a broker's customer; the 2nd Circuit's Pearlstein II holding that there was an implication of a private right of action against a broker for a violation of Regulation T despite the recognition that the amendment of 7(f) caused some doubt as to the validity of the Pearlstein I decision; the 5th Circuit in McCormick-Esposito (500F2d620, 33ALR Fed 614) held:

> "in denying customer relief in this case we do not deprive good faith investors of protection from unscrupulous or overbearing brokerage practices.-----" (1974)(emphasis added)

and the 6th Circuit held that the Petitioner had no private right of action against his broker for the broker's violations of Regulation T affirming the Petitioner's contention of conflicting circuit courts of appeals decisions on private implied rights of action, constituting a reason for the granting of the Certiorari Writ.

If an investor is denied a private right of action the Petitioner asks this Court to

consider that the investor being a borrower under 7(f) and Regulation X and through no fault of his own becomes subject to the penalties of section 32 of the 1934 Act, fine of 10,000 dollars and imprisonment of up to two years should his broker violate the margin requirements. The Court could also take into account the following: Should all investors discover that the federal district and circuit courts generally have held that they do not have a private right of action against their broker for his violation of the margin rules, then it seems inevitable that the margin investor must get out of the market, sell out his holdings, cover his short sales and option transactions and thus cause a repetition of the 1929 market break and the subsequent Great Depression, which culminated in the enactment of the 1933 Securities Act and the 1934 Securities Exchange Act.

The Petitioner calls this Court's attention to the extremely important fact that relates to the many references to section 7(f)

and Regulation X (related to the "obtaining" of credit for the sole purpose of "purchasing securities) and this litigation in general and that is the litigation involves two purchase transactions and sixteen short sale transactions (eleven short sales in stocks and five in options), the short sale transactions not being related to both 7(f) or Regulation X, not being purchases. That is to say, whatever cognition the 6th Circuit gave to 7(f) and Regulation X in its denial of the private right of action to Petitioner could relate to the two purchase transactions only.

The Petitioner contends that this Court's failure to grant his petition for Certiorari can only result in the Respondent and other brokerage houses handling customer accounts similarly to the Respondent believing that a license to steal, cheat and defraud has been received, that the "protection of investors" concept of the 1934 Exchange Act has been declared null and void. This is another reason for the granting of the Certiorari Writ.

The Petitioner calls the attention ofthis Court to a situation that prevails in the federal courts in which the questioning of the validity of its Pearlstein I court's decision implying a private right of action for a violation of section 7 of the 1934 Act and Regulation T, by the Pearlstein II court has been cited by both district and circuit courts as grounds for the denial of an implied private right of action for a violation of section 7 and Regulation T.

It is evident that no consideration was given to the Congressional intent in enacting P.L. 91-508. At Part III of that law it is seen that 1934 section 7 is amended by the addition of subsection (f) at 301 (a); at 301 (b) a savings clause is worded so:

> (b) The amendment made by subsection (a) of this section does not affect the continuing validity of any rule or regulation under section 7 of the Securities Act of 1934 in effect prior to the effective date of the amendment.

The Petitioner who has spent thousands of hours in law libraries researching this litigation knows of no court which has given

consideration to the intent of Congress in enacting the savings clause. Congress was aware of the Pearlstein I court's decision holding a broker solely liable for a violation of Regulation T under section 7(c) of the 1934 Act. In enacting the savings clause of P.L. 91-508, Congress made crystal clear of intent to maintain the "continuing validity" of 7(c) despite the addition of 7(f). The Petitioner alerts this Court to the recognition that 7(f) seemingly placed a "U.S. person" in an unlawful position if the credit he obtained in a security purchase transaction was "prohibited" under Regulation T's margin requirements ; the statutory language of these rules in no way shows that a transaction is for any reason "prohibited"; this is clearly seen by a detailed analysis of Regulation T.

It is imperative that this Court understand that a credit transaction takes place when a customer calls his broker and gives an order to purchase.The broker immediately transmits the order to an exchange or the OTC where the transaction is effected in a matt-

er of minutes. There is nothing in the rules of Regulation T to prevent the broker from "prohibiting" the transaction. Once the transaction is effected, the customer must deposit with the broker his margin requirement within a 5 business day period else the broker must liquidate the transaction previously made.

This Court has never considered questions relating to the Special Miscellaneous Account heretofore, and the great potential for fraud on the customer by his broker.

This Court has never before considered questions relating to the enactment of 7(f) under Public Law 91-508 (Bank Records and Foreign Transactions Act) and its effect on the customer-broker relationship. The concomitant to 7(f), Regulation X of the Federal Reserve Board has also not been adjudicated by the Court. Both 7(f) and Regulation X have been the subject of differing holdings by the federal courts; constituting another reason for a granting of a Certiorari Writ.

This Court has never before made adjudications regarding the Federal Reserve Board's Regulation T and its known complexity which could conceivably result in the "protection of investors" not taking place but that brokers in their own interpretation of the complex Regulation T find ways to place themselves in a " Heads Iwin, tails you lose"

situation, a phrase made famous by Judge Friendly and often cited by Federal courts in cases involving violations of federal securities laws by brokers.

In conclusion, the Petitioner requests this Court to note its many holdings in its BORAK case favoring private rights of action emphasized below by repeating them:

"It appears clear that private parties have a right under para. 27 to bring suit for violation of para. 14(a) of the Act. Indeed this section specifically grants the appropriate District Courts jurisdiction over "all suits in equity and actions at law brought to enforce any liability or duty created" under the Act.

"While this language makes no specific reference to a private right of action, among its chief purposes is "the protection of investors", which certainly implies the availability of judicial relief where necessary to achieve that result."

"Private enforcement of the proxy rules provides a necessary supplement to Commission action."

"We, therefore, believe that under the circumstances here it is the duty of the courts to be alert to provide such remedies as are necessary to make effective the congressional purpose."

"It is for the federal courts" to adjust their remedies so as to grant the necessary relief" where federally secured rights are invaded." And it is also well settled that where legal rights have been invaded, and a federal statute provides for a general right to sue for such invasion, federal courts may use any available remedy to make good the wrong done."

"Section 27 grats the District Court's jurisdiction of "all suits in equity and actions at law brought to enforce any liability or duty created by this title ..." In passing on almost identical language in the Securities Act of 1933, the Court found the words entirely sufficient to fashion a remedy to rescind a fraudulent sale, secure restitution and even to enforce the right to restitution against a third party holding assets of the vendor."

"The power to enforce implies the power to make effective the right of recovery afforded by the Act. And the power to make the right of recovery effective implies the power to utilize any of the procedures or actions normally available to the litigant according to the exigencies of the particular case."

This Court should grant the Petition for Certiorari so that as the Banking Law Journal article states "Hopefully, one day the the U.S. Supreme Court will resolve the question once and for all."

In one of his previously asked questions of this Court the Petitioner has mentioned the possible mootness of its 4-pronged holding as to an implicit right of action in its CORT-ASH case; thus, the Petitioner, in possibly repeating what he has said heretofore, calls the attention of the Court to its holding in BORAK in which it recognized that section 27 of the 1934 Act stated federal court jurisdiction but also private rights for actions at law explicitly for violations of the Act and the rules and regulations thereunder; thus indicating another reson for granting of the Certiorari Writ.

Furthermore, referring to this Court's CORT-ASH case at the syllabus at 2(a) it is stated:

> "Section 610 was primarily concerned, not with the internal relations between the corporations and stockholders, but with corporations as a source of aggregated wealth and therefore of potential corrupting influence; thus this statute differs from other criminal statutes in which private causes of action have been inferred because of a clearly articulated federal right in the plaintiff,---- or a pervasive legislative scheme governing the relationship between the the plaintiff class and the defendant class in a particular regard, e.g., J.I.CASE CO. v. BORAK, 377 U.S. 426

Pp.78-82.(emphasis added)

Thus, one more reason for the granting of the Petitioner's Certiorari Writ.

The Petitioner, believing that it would be helpful to the Court requests the Court's permission for leave to file with this petition, that is to lodge with the Court, Two amici involved in the STERN- MERRILL,LYNCH case (603 F.2d 1073) in which both the Securities and Exchange Commission and the Federal Reserve Board express their views favorable to the implication of private rights of action and an amicus of the S E C in SCHY et al v. FEDERAL DEPOSIT INSURANCE CORP., et al (CCH paragraph 96,242) favoring an implied private right of action. In addition, the Petitioner lodges with the Court a press release of the S E C of August 31, 1980 titled "Information for Investors" regarding "buying power"; an issue which lies at the heart of this case; the significant portion being: "The SMA is one of the most important, yet least understood, special accounts which exist under the req-

uirements of Regulation T of the Federal Reserve System."; and " There is no specific formula or computation that a customer can use to arrive at his SMA balance. It can be done only by tracing the history of the account and examining all entries made over the life of the account. However, a customer's SMA may never have a debit balance. The account must contain either a credit or a zero balance."

This is brought to the attention of the Court for its recognition of the impossibility of the Petitioner or any investor for that matter to have knowledge as to whether his broker is following the "provisions" of Regulation X or not, thus adding another reason for granting the petition for Certiorari.

In addition, it has come to the attention of the Petitioner that the Congress has held hearings on H.R. 1294 on February 26 and April 2 of this year in which subsection 7(f) is to be amended; 7(f) having played a crucial role in the Sixth Circuit's holding that the Petitioner had no implied private right

of action against the Respondent; this development could be beneficial to the Court in giving it a perspective on the intent of Congress from the original enactment of 7(f) in P.L. 91-508 and its present intent in H.R. 1294 of allowing an explicit private right of action. Reference to the above is:

HEARINGS
before the
SUBCOMMITTEE ON TELECOMMUNICATIONS,
CONSUMER PROTECTION, AND FINANCE
of the
COMMITTEE ON ENERGY AND COMMERCE
HOUSE OF REPRESENTATIVES
Ninety-Seventh Congress
First Session
H.R.1294

A bill to amend the Securities and Exchange Act of 1934 to provide uniform margin requirements in transactions involving the acquisition of securities of certain United States corporations by non-United States persons where such acquisition is financed by non-United States lenders.

February 26 and April 2, 1981
SERIAL NO. 97-2
Printed for the use of the
Committee on Energy and Commerce

The attention of this Court is directed especially to the letter of Acting Chairman Loomis of the S E C on pages 89 and following stating the S E C's concepts regarding the relationships involving 7(f), the var-

ious courts and their differing interpretations of private rights of action under 7(f); even the citing of the Petitioner's case before the Sixth Circuit.(note 3, page 93)

Worthy of note also is the letter of J. Charles Partee, member of the Federal Reserve Board on pages 101 and 102 commenting on the Board's friend of the court briefs "recognizing private enforcement of the margin requirements". The preceding two paragraphs constitute another in the many reasons that the Petitioner believes should result in a clearcut justification of the granting of this Writ of Certiorari.

The Petitioner has just received information on Sep. 21, 1981 that the Energy & Commerce Committee has passed H.R. 4145 on Sep. 17, 1981. H.R 4145 reads:

A BILL

To amend the Securities Exchange Act of 1934 to provide uniform margin requirements in transactions involving the acquisition of securities of certain United States corporations by non-United States persons where such acquisition is financed by non-United States lenders, to specify a private right of action for violations of margin requirements, and for certain other purposes.

It is the Petitioner's intention in citing both the H.R. 1294 Hearings and H.R. 4145 passage to alert the Court that the controversial 7(f) amendment of 1970 is now being again amended to clarify its previous ambiguosity and to make explicit a private right of action; thus making it both fitting and proper that this Court should see another reason for the granting of the Petitioner's Certiorari Writ.

By the granting of this Writ this Court can once and for all end the differences of opinions of the Federal district and circuit Courts respecting interpretations of 7(f) and both implicit and explicit private rights of action by customers of brokers who violate Section 7 of the 1934 Securities Exchange Act and Regulation T of the Federal Reserve Board promulgated thereunder.

Respectfully submitted,

Phil Gutter

Philip Gutter, Petitioner,
Non-Lawyer

CERTIFICATE OF SERVICE

I hereby certify that I will hand deliver to the office of John Witten, 250 E. Broad St., Columbus, Ohio, 3 copies of this PETITION FOR A WRIT OF CERTIORARI immediately upon printing thereof.

Philip Gutter

Philip Gutter, Petitioner

APPENDIX- (A1)

SECTION 17(a)- 1933 SECURITIES ACT

"It shall be unlawful for any person in the offer or sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly-

(1) to employ any device, scheme, or artifice to defraud, or

(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any transaction, practice, or cource of business which operates or would operate as a fraud or deceit upon the purchaser.

SECTION 22(a)- 1933 Securities Act

"The district courts of the United States, the United States courts of any Territory, and the United States District Court for the District of Columbia shall have jurisdiction of offenses and violations under this title and under the rules and regulations promulgated by the Commission in respect thereto, and concurrent with State and Territorial courts, of all suits in equity and actions at law brought to enforce any liability or duty created by this title.-----.

SECTION 7(a)- 1934 SECURITIES EXCHANGE ACT

"For the purpose of preventing the excessive use of credit for the purchase or carrying of securities, the Board of Governors of the Federal Reserve System shall, prior to the effective date

of this section and from time to time thereafter, prescribe rules and regulations with respect to the amount of credit that may be initially extended and subsequently maintained on any security (other than an exempted security). ....."

SECTION 7(c)- 1934 SECURITIES EXCHANGE ACT

"It shall be unlawful for any member of a national securities exchange or any broker or dealer, directly or indirectly to extend or maintain credit or arrange for the extension or maintenance of credit to or for any customer--
(1) on any security (other than an exempted security), in contravention of the rules and regulations which the Board of Governors of the Federal Reserve System shall prescribe under subsections (a) and (b) of this section;
-------"

SECTION 7(d)(E)- 1934 SECURITIES EXCHANGE ACT

"to such other loans as the Board of Governors of the Federal Reserve System shall, by such rules and regulations as it may deem necessary or appropriate in the public interest or for the protection of investors, exempt, either unconditionally or upon specified terms and conditions or for stated periods, from the operation of this subsection and the rules and regulations thereunder"

SECTION 7(f)- 1934 SECURITIES EXCHANGE ACT

"It is unlawful for any United States person, or any foreign person controlled by a United States person or acting on behalf of or in conjunction with such

person, to obtain, receive or enjoy the beneficial use of a loan or other extension of credit from any lender (without regard to whether the lender's office or place of business is in a State or the transaction occurred in whole or in part within a State) for the purpose of (A) purchasing or carrying United States securities or (B) purchasing or carrying within the United States of any other securities, if, under this section or rules and regulations prescribed thereunder, the loan or other credit transaction is prohibited or would be prohibited if it had been made or the transaction had otherwise occurred in a lender's office or other place of business in a State".

PUBLIC LAW 91-508- MARGIN REQUIREMENTS-- PARA. 301-- AMENDMENT OF SECTION 7 OF THE SECURITIES EXCHANGE ACT OF 1934

(a) --------.
(b) "The amendment made by subsection (a) of this section does not affect the continuing validity of any rule or regulation under section 7 of the Securities Exchange Act of 1934 in effect prior to the effective date of the amendment".

SECTION 10(b)(5)--SECURITIES & EXCHANGE COMMISSION RULES-- EMPLOYMENT OF MANIPULATIVE AND DECEPTIVE DEVICES

"It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
(a) To employ any device, scheme, or artifice to defraud,
(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the state-

ments made, in the light of the circumstances under which they were made not misleading, or
(c) To engage in any act,practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security".

SECTION 27--SECURITIES EXCHANGE ACT OF 1934
JURISDICTION OF OFFENSES AND SUITS

"The district courts of the United States, the United States District Court for the District of Columbia, and the United States courts of any Territory or other place subject to the jurisdiction of the United States shall have exclusive jurisdiction of violations of this title or the rules and regulations thereunder, and of all suits in equity and actions at law brought to enforce any liability or duty created by this title or the rules and regulations thereunder. ----------."

SECTION 29--SECURITIES EXCHANGE ACT OF 1934
VALIDITY OF CONTRACTS

(a) Any condition, stipulation, or provision binding any person to waive compliance with any provision of this title or of any rule or regulation thereunder, or of any rule of an exchange required thereby shall be void..

(b) Every contract made in violation of any provision of this title or of any rule or regulation thereunder, and every contract (including any contract for listing a security on an exchange) heretofore or hereafter made the performance of which involves the violation of, or the continuance of any relationship or practice in violation of, any provision of this title or any rule or regulation thereunder shall be void (1) as regards the rights of any person who, in violation of any such pro-

vision, rule, or regulation, shall have made or engaged in the performance of any such contract, and (2)------."

FEDERAL RESERVE BOARD REGULATION "T"--SECTIONS PERTINENT TO THIS PETITION. 12 C.F.R. PART 220

220.3(a) CONTENTS OF GENERAL ACCOUNT. All financial relations between a creditor and a customer, whether recorded in one record or in more than one record, shall be included in and be deemed to be part of the customer's general account with the creditor, except that the relations which para. 220.4 permits to be included in any special account provided for by that section may be included in the appropriate special account, and all transactions in commodities, and, except to the extent provided in para. (b)(2) of this section, all transactions in non-equity securities, exempted securities, and in other securities having no loan value in a general account under the provisions of paragraph (c) of this section and para. 220.8 (the Supplement to Regulation T) (except unissued securities, short sales, and security positions to offset short sales other than those permitted in para. 220.4(j)(5), purchases to cover short sales and contracts involving an endorsement or guarantee of any put, call, or other option, shall be included in the apprpriate special account provided for by para. 220.4. -----.

(b) GENERAL RULE. (1)(i) A creditor shall not effect for or with any customer in a general account, special bond account subject to para. 220.4(i), or special convertible debt security account any transaction which, in combination with the other transactions effected in such account on the same day, creates an excess of the adjusted debit balance of such

account over the maximum loan value of the securities in such account, or increases any such excess, unless in connection therewith the creditor obtains, as promptly as possible and in any event before the expiration of 5 full business days following the date of such transaction, the deposit into such account of cash or securities in such amount that the cash deposited plus the loan value of the securities deposited equals or exceeds the excess so created or the increase so caused.(ii) ----.(2)-------.(3) Rules for computing the maximum loan value of the securities in a general account, special bond account, or special convertible security account and the adjusted debit balance of such account are provided in paragraphs (c) and (d) of this section, and certain modification and exceptions to the general rule stated in this paragraph are provided in the subsequent paragraphs of this section and in para. 220.6.

(c) MAXIMUM LOAN VALUE AND CURRENT MARKET VALUE. (1) ------.(2)----. No collateral other than an exempted security or a registered nonequity security held in such account on March 11, 1968, and continuously thereafter, or margin equity security shall have any loan value in a general account except that a margin equity security eligible for a special convertible security account pursuant to para. 220.4(j) shall have loan value in a general account only if held in the account on March 11, 1968, and continuously there after. (3)-----.(4) For the current market value of a security throughout the day of its purchase or sale, the creditor shall use its total cost or the net proceeds of its sale, as the case may be and at any other time shall use the closing sale price of the security on the preceding business day as shown by any regularly published reporting or quotation service. ---.

(d) ADJUSTED DEBIT BALANCE.- For the purpose of this part, the adjusted debit balance of a general account, special bond account, or special convertible debt security account shall be calculated by taking the sum of the following items:

(1) The net debit balance, if any, of such account;

(2) The total cost of any securities (other than unissued securities) bought for such account but not yet debited thereto;

(3) The current market value of any securities --- sold short---;

(4) ------;

(5) The amounts of any margin required in connection with the issuance, endorsement, or guarantee of any put, call or combination thereof;

(6) The net credit balance, if any, of such account; and

(7) The net proceeds of any sale of securities--- sold for such account but for which payment has not yet been credited thereto. -----.

(e) LIQUIDATION IN LIEU OF DEPOSIT. In any case in which the deposit required by paragraph (b) of this section, or any portion thereof, is not obtained by the creditor within the 5-day period specified therein, margin nonexempted securities shall be sold (or, to the extent that there are insufficient margin nonexempted securities in the general account,-----other liquidating transactions shall be effected in such account) prior to the expiration of such 5-day period, in such amount that the resulting decrease in the adjusted debit balance of such account exceeds, by an amount at least as great as such required deposit or the undeposited portion thereof, the "retention requirement" of any margin or

exempted securities sold: PROVIDED, That a creditor is not required to sell securities or to effect other liquidating transactions specified by this paragraph in an amount greater than necessary to eliminate the excess of the adjusted debit balance of such account over the maximum loan value of the securities remaining in such account after such liquidation.

PARAGRAPH 220.4 --SPECIAL ACCOUNTS

(a) GENERAL RULE. (1) Pursuant to this section, a creditor may establish for any customer one or more special accounts. (2) Each such special account shall be recorded separately and shall be confined to the transactions and relations specifically authorized for such account by the appropriate paragraph of this section and to transaction and relations incidental to those specifically authorized. An adequate record shall be maintained showing for each such account the full details of all transaction in the account. (3) A special account established pursuant to this section shall not be used in any way for the purpose of evading or circumventing any of the provisions of this part. If a customer has with a creditor both a general account and one or more special accounts, the creditor shall treat each such special account as if the customer had with the creditor no general account, special bond account subject to paragraph 220.4(i), or convertible security account subject to paragraph 220.4(j).

(i) SPECIAL BOND ACCOUNT. In a special bond account a creditor may effect and finance transactions in exempted securities and registered nonequity securities for any customer.

PARAGRAPH 220.8 SUPPLEMENT

(a) MAXIMUM LOAN VALUE FOR GENERAL ACCOUNTS. The maximum loan value of securities in a general account subject to paragraph 220.3 shall be:

(1) Of a registered non-equity security held in the account on March 11, 1968, and continuously thereafter, and of a margin equity security (except as provided in 220.3(c) and paragraphs (b), (c), and (f) of this section), 50 per cent of the current market value of such securities.

(2) ------.

(b) MAXIMUM LOAN VALUE FOR A SPECIAL BOND ACCOUNT. The maximum loan value of an exempted security and of a registered non-equity secured pursuant to 220.4(i) shall be the maximum loan value of the security as determined by the creditor in good faith.

No. 79-3516

No. 79-3517

UNITED STATES COURT OF APPEALS

FOR THE SIXTH CIRCUIT

PHILIP GUTTER

Plaintiff-Appellant
Cross-Appellee

v.

MERRILL, LYNCH, PIERCE,
FENNER & SMITH, INC.

Defendant-Appellee
Cross-Appellant

Decided and Filed April 3, 1981

Before MERRITT, BROWN and KENNEDY,
Circuit Judges.
BAILEY BROWN, J.

I

This case grows out of a series of margin transactions executed by appellee and cross appellant, Merrill, Lynch, Pierce, Fenner, & Smith, Inc. (Merrill Lynch), on behalf of appellant and cross-appellee, Philip Gutter (Gutter), in September and October of 1974. Gutter made a number of short

sales and wrote a number of option contracts through his broker Merrill Lynch, all on margin. Although some of the short sales were successful, most of the transactions resulted in losses to Gutter. To finance his margin trading Gutter deposited $122,000 in corporate bonds in a special account with Merrill Lynch. All of Gutter's trades were financed with loans Merrill Lynch made against the collateral of the bonds.

Gutter brought this action to recover his losses from Merrill Lynch, and in his amended complaint stated two types of claims. First, Gutter claimed that Merrill Lynch had violated the anti-fraud provisions of the Securities Act of 1933, 15 U.S.C. paragraphs 77 et seq., and the Securities Exchange Act of 1934, 15 U.S.C. paragraphs 78 et sec., and had committed common law fraud by failing to fully inform him of the risks involved in option trading. He also alleged that Merrill Lynch misrepresented the profits that could be obtained from option trading.

Second, Gutter claimed that Merrill Lynch had violated the margin requirements of Section 7(c) of the 1934 Act, 15 U.S.C. paragraph 78 (c), and the regulation implementing Section 7(c), Federal Reserve Board Regulation T, 12 C.F.R. paragraphs 220.1 et seq., by using his bonds in the special account as collateral for his margin trading rather than calling on Gutter to cover the shortfalls in his margin account. He claimed that Merrill Lynch was liable to him for his losses in the margin account.

As an initial matter the district court granted Gutter's motion for summary judgment on the Regulation T claims On the authority of our decision in SPOON v. WALSTON & CO., 478 F.2d 246(6th Cir. 1973), the district court held that an implied cause of action existed for a violation of the margin regulations. The district court then found, as Gutter contended, that Merrill Lynch had violated the margin requirements by applying the excess value of Gutter's bonds to his margin account instead of issuing maintenance

calls at times when the margin limitations were exceeded. On the basis of stipulated underlying facts, damages were determined by the court to be $7000.

Gutter's fraud claims were tried to a jury on May 1, 1978. The district court granted a directed verdict for Merrill Lynch on Gutter's claim that Merrill Lynch had violated Sections 12(2) and 17(a) of the 1933 Act, 15 U.S.C. paragraphs 771(2), 77q(a). The court noted that the protection of these sections was clearly limited to purchasers and, as an option writer, Gutter was plainly a seller and not a purchaser. The 1934 Act and common law fraud claims were submitted to the jury, which returned a verdict for Merrill Lynch.

Gutter has appealed the district court's directed verdict on his fraud claims under the 1933 Act and appealed the method used to calculate damages for Merrill Lynch's violation of the margin requirements of Regulation T. Merrill Lynch appeals both the finding that it violated the margin require-

ments and the holding that a violation of the margin requirements gives rise to a private cause of action. Merrill Lynch also appeals the calculation of damages flowing from the alleged violations.

We determine that the district court did not err in directing a verdict on the fraud claims under the 1933 Act. We determine, however, that the district court erred in granting summary judgment to Gutter and in awarding him damages for violations of the margin requirements of Regulation T for the reason that a private cause of action cannot be implied for a violation of Regulation T and the statute pursuant to which the regulation was issued. Since we determine that the private cause of action cannot be implied, we need not decide whether Regulation T was violated by Merrill Lynch or whether the district court applied the correct measure of damages for such violation.

II

Gutter's claims under the 1933 Act related only to his option transactions. It is clear that only purchasers have standing un-

der Sections 12(2) and 17(a) of the 1933 Act. These provisions simply are not designed to protect sellers, and this is obvious from the face of the statutes. They have also been consistently interpreted to provide protection only to purchasers. See e. g. Simmons v. Wolfson, 428 F. 2d 455 (6th Cir. 1970)(per curiam), cert. denied, 400 U.S. 999 (1971).

It is furthermore obvious that with regard to the option contracts Gutter was a seller and not a purchaser. Under the terms of the Chicago Board Options Exchange Clearing Corporation (CBOE), whose options Gutter was writing, the writer receives a premium and agrees to deliver the underlying security to the CBOE on call at a fixed price. The option price of the underlying security is always above the market price at the time the option is written. The writer hopes the market price will not rise above the option price so the holder of the option will not exercise it. If the price of the security risesabove the option price, the holder will exercise the option since he can make an immediate profit by selling the stock he purchased at the lower

option price at the then higher market price. If the option is uncovered (i.e., the option writer does not already own the shares) the writer will have to cover by purchasing securities at the existing market price and delivering them at the lower option price. The option writer makes the same gamble as a short seller in that he hopes the market will go down over the life of the option. If the market declines he makes a profit (the premium the purchaser paid for the option) and does not have to purchase or sell the underlying security. It is clear that an option writer sells the right to purchase securities and is not purchasing anything. The fact that he may have later to purchase securities to cover his option is irrelevant to the determination of whether the writing of the option contract is itself a purchase or sale. The district court correctly determined that Gutter was a seller with regard to the option contracts. Although the anti-fraud provisions of the 1934 Act protect both purchasers and

sellers, the anti-fraud provisions of the 1933 Act protect only purchasers. Therefore, the district court correctly granted a directed verdict for Merrill Lynch on the 1933 Act claims.

III

We next turn to the question whether a private cause of action can be implied in favor of a broker's customer against the broker for a violation of the margin requirements established by Regulation T issued pursuant to Section 7(c) of the 1934 Act.

The district court, apparently with some reluctance, concluded that a private cause of action must be implied. It pointed out that the implication of a cause of action means that, so far as the customer is concerned, it is "heads I win, tails you lose" where there is a loss in a margin account. The district court concluded that this result was compelled by the per curiam decision of this court in Spoon v. Walston & Co., 478 F. 2d 246 (6th Cir. 1973). We conclude, however, that under the circumstances presented here that Spoon is not controlling and a private cause of

action cannot be implied. The reasons why we conclude that Spoon is not controlling are: (1) an amendment to Section 7 of the 1934 Act that was not applicable to the transactions involved in Spoon is applicable here;(2) in a recent decision this court indicated that the rule followed in Spoon may, in the light of more recent decisions in other courts, no longer be viable; and,(3) recent decisions of the Supreme Court establishing standards for the implication of private causes of action from criminal or regulatory statutes make clear that a private cause of action should not be implied here.

In 1970, Section 7 of the 1934 Act was amended by adding Section 7(f). which made it illegal for customers of brokers to accept credit in excess of limits permitted by the margin requirements of the regulation issued pursuant to Section 7. Prior to the enactment of Section 7(f), it had been illegal,under Section 7(c), for brokers to extend excess credit but not illegal for customers to accept it. The amendment placed the responsibil-

ity on both the broker and the customer to observe the margin requirements. The Federal Reserve Board issued Regulation X, 12 C.F.R. paragraphs 224 et seq., to effectuate this change in the law.

The margin transactions involved in Spoon took place in 1971, and the broker contended in the district court, inter alia, that the addition in 1970 of Section 7(f) to the Act prevented the implication of a cause of action in favor of the customer. The district court in Spoon recognized this argument in its opinion, 345 F. Supp. 518, 521-22 (E.D. Mich. 1972), but pointed out that the amendment did not take effect until after the margin transactions involved in the case had taken place. It then concluded that a private cause of action in favor of the customer against the broker must be implied. Even so, and even though the broker had been guilty of fraud on the New York Stock Exchange in covering up its violations of the margin requirements, the district court, applying equitable principles,

allowed the customer to recover only one-half of the loss incurred in the margin account.

In its brief per curiam affirming the district court in Spoon, 478 F.2d 246(6th Cir. 1973), this court relied principally on Pearlstein v. Scudder & German, 429 F.2d 1136(2nd Cir. 19700(Pearlstein I), cert. denied, 401 U.S. 1013(1971), saying:" We agree with the Second Circuit that Congress intended for the loss in transactions of this type generally to fall upon the broker". 478 F.2d at 247. Pearlstein I, like Spoon, dealt with transactions to which the 1970 amendment (Section 7(f)) did not apply.

In Utah State University v. Bear, Stearns & Co., 549 F.2d 164(10th Cir.), cert denied, 434 U.S. 890(1977), the court held that as the 1970 amendment to the 1934 Act(Section 7(f)) and Regulation X were applicable to the transactions involved, no private cause of action in favor of the broker's customer could be implied. It pointed out that Section 7(f) and Regulation X were not applicable to the transactions involved in Pearlstein I and Spoon. The 10th Circuit also pointed out that

when Pearlstein came before the Second Circuit again on the question of damages,527 F.2d 1141,1144(2nd Cir. 1975)(Pearlstein II), the Second Circuit recognized that since the advent of the 1970 amendment and Regulation X, its prior decision holding that a private cause of action must be implied was of doubtful validity.

In Stern v. Merrill, Lynch, Pierce, Fenner & Smith, Inc., 603 F.2d 1073(4th Cir. 1979), the court, after reviewing at length the history of litigation on this issue, came to the generally accepted conclusion that the overall purpose of Section 7(c) and Regulation T, as macroeconomic policy, was to control the quantum of credit in the economy. It came to the further conclusion that, with the enactment of Section 7(f) and Regulation X, it could no longer be said that even an ancillary purpose of Section 7(c) was to protect customers of brokers from losses that occurred where margin requirements were violated. Accordingly, the court concluded that a private cause of action could not be implied in favor of the customer.

In Fryling v. Merrill, Lynch, Pierce, Fenner & Smith, Inc., 593 F.2d 736(6th Cir.), this court determined that the broker that had been sued by a customer on the basis of an alleged violation of Section 7(c) and Regulation T had not in fact violated those provisions and, therefore, it was not necessary for this court to determine whether a private cause of action could be now implied. This court pointed out there were contrasting views on this issue, inviting comparison of Pearlstein I, on which it had relied in Spoon, with Pearlstein II and Utah State University. Id at 745,n. 8.

Beginning with Cort v. Ash, 422 U.S.66 (1975), the Supreme Court has set down more stringent rules for implying private causes of action for violation of criminal and regulatory statutes. In Cort, the Court stated the rules to be: whether plaintiff is one of a class for whose especial benefit the statute was enacted; whether there is an indication of legislative intent to create a private remedy; whether implication of a private rem-

edy is consistent with the legislative purpose; and whether such a cause of action is traditionally relegated to state law. Id at 78 In Touche Ross & Co. v. Redington, 442 U.S. 560 (1979),the Court stated that it did not intend by its holding in Cort to give equal weight to all four of the aforementioned factors, and that the central inquiry was whether Congress intended to create a private cause of action. Id at 575.

In Piper v. Chris-Craft Industries, Inc., 430 U.S. 1(1977), the Court stated that the threshold issue was whether a tender offeror such as Chris-Craft, whose activities were regulated by the Williams Act, 15 U.S.C. paragraph 78m(d)(1), had a cause of action for damages against other parties whose activities were regulated by the Act, on a claim that violations of the Act by other parties frustrated the tender offeror's(Chris-Craft's) efforts to obtain control of the target corporation. Id at 24. In answering this question in the negative, the Court, referring to

Cort, stated, inter alia:

> There, the Court identified four factors as "relevant" in determining whether a private remedy is implicit in a statute not expressly providing one. The first is whether the plaintiff is " 'one of the class for whose especial benefit the statute was enacted ... ..' " Id., at 78, 45 LEd 2d 26, 95 S Ct 2080. (emphasis in original) As previously indicated, examination of the statute and its genesis shows that Chris-Craft is not an intended beneficiary of the Williams Act, and surely is not one "for whose especial benefit the statute was enacted." Ibid. To the contrary, Chris-Craft is a member of the class whose activities Congress intended to regulate for the protection and benefit of an entirely distinct class, shareholders-offerees. As a party whose previously unregulated conduct was purposefully brought under federal control by the statute, Chris-Craft can scarcely lay claim to the status of "beneficiary" whom Congress considered in need of protection. Id at 37.

Applying these decisions to the instant case, we conclude that they do not permit the implication of a private cause of action in favor of Gutter. In the light of the enactment of the 1970 amendment to the 1934 Act (Section 7(f)) and the issuance of Regulation X, Gutter is not in a class for whose especial benefit this statute was enacted and, indeed, Gutter is a party whose conduct has been brought under control by the statute. Moreover there is no indication of Congressional intent to create a cause of action in favor of

the broker's customer against the broker, and the enactment of Section 7(f) indicates a contrary intent.

We therefore conclude that the judgment of the district court should be affirmed insofar as it denied relief to Gutter. We further conclude that the judgment of the district court must be reversed insofar as it granted relief to Gutter. The cause is remanded to the district court with direction to enter a judgment dismissing the action with prejudice. No costs assessed.

Opposition

Office-Supreme Court, U.S.
FILED
DEC 30 1981
ALEXANDER L. STEVAS,
CLERK

No. 81-965

In the Supreme Court of the United States

October Term, 1981

PHILIP GUTTER
Petitioner,

vs.

MERRILL LYNCH, PIERCE, FENNER & SMITH, INC.
Respondent

Brief For Respondent In Opposition To Petition For Writ Of Certiorari To The United States Court Of Appeals For The Sixth Circuit

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2. Whether § 12(2) or §17(a) of the Securities Act of 1933 affords a remedy to a seller of options contracts against his broker?

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No. 81-965

In the Supreme Court of the United States

October Term, 1981

PHILIP GUTTER
Petitioner,

vs.

MERRILL LYNCH, PIERCE, FENNER & SMITH, INC.
Respondent

Brief For Respondent In Opposition To Petition For Writ Of Certiorari To The United States Court Of Appeals For The Sixth Circuit

The respondent Merrill Lynch, Pierce, Fenner & Smith, Inc. ("Merrill Lynch")[1] respectfully submits this Brief in Opposition to the Petition for Writ of Certiorari.

OPINIONS BELOW

The opinion of the Court of Appeals for the Sixth Circuit (the "Court of Appeals") is reported at 644 F.2d 1194 (6th Cir. 1981) and is reproduced in the Petitioner's Appendix. The opinion and order of the District Court for the Southern District of Ohio, Eastern Division (the "District Court") granting the partial summary judgment in favor of the petitioner is reported at [1977-1978] Fed. Sec. L. Rep. (CCH) ¶ 96,239 (S.D. Ohio, September 9 and November 23, 1977).

[1] Pursuant to Rule 28.1 of this Court, Merrill Lynch states that it is a wholly owned subsidiary (except for qualifying shares) of Merrill Lynch & Co., Inc., and that neither it nor its parent have any significant subsidiaries and affiliates other than wholly owned subsidiaries and affiliates (except for qualifying shares) and Merrill Lynch International Bank Incorporated, a 95% owned subsidiary of Merrill Lynch & Co., Inc.

JURISDICTION

The judgment of the Court of Appeals was entered on April 3, 1981, the petitioner's petition for rehearing *en banc* was denied on May 15, 1981 and the petitioner's motion for reconsideration of the denial for rehearing *en banc* was denied on June 24, 1981. The petitioner received extensions of time to file his petition first to September 14, 1981, by an order dated July 21, 1981, and then to October 12, 1981, by an order dated September 3, 1981. This Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

QUESTIONS PRESENTED

The petition presents nineteen separate questions for determination by this Court. However, the respondent believes that this formidable list can fairly be collapsed into the two essential questions decided by the Court of Appeals.

1. Whether there is an implied private remedy by a customer against his stock broker for violations of Federal Reserve Board Regulation T promulgated under § 7 of the Securities Exchange Act of 1934?
2. Whether § 12(2) or § 17(a) of the Securities Act of 1933 affords a remedy to a seller of options contracts against his broker?

STATEMENT OF CASE

The petitioner, Mr. Philip Gutter, brought this action for the purpose of recouping stock market trading losses from his stock broker, Merrill Lynch, the respondent. Mr. Gutter realized these trading losses in a series of transactions, which include a number of short sales, sales of options contracts and a few purchases of stock, which Merrill Lynch executed for his account in September and October, 1974. Mr. Gutter furnished margin collateral for

these transactions by depositing approximately $122,000 in corporate bonds in his account with Merrill Lynch. A portion of these bonds were subsequently liquidated in order to effect covering transactions for Mr. Gutter's unsuccessful short sales and sales of uncovered options contracts.

The petitioner's primary complaint against Merrill Lynch was that his Merrill Lynch representative fraudulently enticed him to sell uncovered options contracts through the Chicago Board Options Exchange. He based these fraud claims on § 12(2) and § 17(a) of the Securities Act of 1933 (the "1933 Act"), 15 U.S.C. §§ 77l(2) and 77q(a), § 10b and Rule 10b-5 under the Securities Exchange Act of 1934 (the "1934 Act"), 15 U.S.C. § 78j(b) and 17 C.F.R. § 240.10.b-5, and the Ohio common law of fraud. The District Court rendered a directed verdict dismissing Mr. Gutter's claims under § 12(2) and § 17(a) of the 1933 Act on the grounds that those provisions were not intended to and did not afford a remedy to sellers of options contracts or other securities. The Court of Appeals affirmed this holding. The remaining fraud claims were disposed of by the jury's verdit in favor of Merrill Lynch and were not the subject of Mr. Gutter's appeal.

The secondary claim raised by Mr. Gutter was that the use of the bonds deposited in his account as margin collateral for his short sales, sales of options contracts, and stock purchases violated Federal Reserve Board Regulation T, 12 C.F.R. § 240.1 *et seq.* promulgated under § 7 of the 1934 Act, 15 U.S.C. § 78g. The District Court rendered a partial summary judgment in favor of Mr. Gutter holding that Merrill Lynch was liable for violations of Regulation T in connection with Mr. Gutter's short sales and purchases of stock and later assessed $7,000 in damages. Mr. Gutter voluntarily dismissed his margin claims in connection with his sales of options contracts prior to the trial. The Court of

Appeals found it unnecessary to review whether or not Merrill Lynch's margin practices violated Regulation T because it held that there was no implied private remedy for such violations.

REASONS FOR DENYING THE WRIT

1. Implied Private Right of Action Under § 7 of the 1934 Act

The petitioner has failed to advance any special or important reasons why this Court should review the question of implying a private right of action under § 7 of the 1934 Act. Instead, Mr. Gutter has simply asserted that this is an important and unsettled question of federal securities law, and has implied that the decision of the Court of Appeals refusing to imply such a private right of action is in conflict with a substantial, albeit aging, body of federal appellate decisions.

In fact, the question is far from unsettled. Beginning with its signal decision in *Cort v. Ash*, 422 U.S. 66 (1975) this Court has devoted considerable judicial attention to settling the standards for the implication of private remedies under federal regulatory statutes, particularly under the federal securities laws. In this process, this Court has evolved increasingly precise and stringent standards for the implication of private rights of action. As a result, neither the Court of Appeals below nor the Courts of Appeals for the Fourth Circuit and the Tenth Circuit, the other two appellate courts which have reviewed the question of implying a private right of action under § 7 of the 1934 Act since this Court's decision in *Cort v. Ash*, have had any difficulty in applying these standards to deny such an implied private remedy under § 7 of the 1934 Act.

In deciding that there was no implied private right of action by a customer against his stockbroker under § 7 of

the 1934 Act for violations of Regulation T, the Court of Appeals overruled its earlier decisions in *Spoon v. Walston & Co.*, 478 F.2d 246 (6th Cir. 1973), and *Goldman v. Bank of the Commonwealth*, 467 F.2d 439 (6th Cir. 1972). These decisions had adopted without elaboration the rule in *Pearlstein v. Scudder & German* ("*Pearlstein I*"), 429 F.2d 1136 (2nd Cir. 1970), *cert. den.*, 401 U.S. 1013 (1971). Prior to this Court's decision in *Cort v. Ash*, *Pearlstein I* was the leading decision implying a private right of action under § 7 of the 1934 Act and, by 1975, it had attracted a following in the Courts of Appeals for the First Circuit, *Landry v. Hemphill, Noyes & Co.*, 473 F.2d 365 (1st Cir. 1973), *cert. den.*, 414 U.S. 1002 (1973), *reh. den.*, 415 U.S. 960 (1974), the Fifth Circuit, *McCormick v. Esposito*, 500 F.2d 620 (5th Cir. 1974), *cert. den.*, 420 U.S. 912 (1975), and the Eighth Circuit, *Naftalin & Co. v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 469 F.2d 1166 (8th Cir. 1972), as well as the Sixth and Second Circuits.

In the decision below, the Court of Appeals refused to follow *Pearlstein I*. Instead, the Court of Appeals applied the four standards for implication of private rights of action first established by this Court in *Cort v. Ash:*

> (i) *Especial Benefit.* "Is the plaintiff 'one of the class for whose *especial* benefit the statute was enacted' – that is, does that statute create a federal right [of action] in favor of the plaintiff?"
>
> (ii) *Legislative Intent.* "... [I]s there any indication of legislative intent, explicit or implicit, either to create such a remedy or to deny one?"
>
> (iii) *Legislative Scheme.* ". . . [I]s it consistent with the underlying purposes of the legislative scheme to imply such a remedy for the plaintiff?"
>
> (iv) *Comity.* ". . . [I]s the cause of action one traditionally relegated to state law, in an area basically the concern of the States, so that it would be inap-

> propriate to infer a cause of action based solely on federal law?"
>
> [422 U.S. at 78 (emphasis in the original) (citations omitted).]

Moreover, as the Court of Appeals noted, during the six years since *Cort v. Ash*, this Court has continued to refine and restrict these four factors. In *Cannon v. University of Chicago*, 441 U.S. 677 (1979), this Court said that the especial benefit factor was a "threshold question" to the implication of a private right of action. 441 U.S. at 689. And, in *Touche Ross & Co. v. Redington*, 442 U.S. 560 (1979), this Court went on to hold that Congressional intent as evidenced by three elements "[i] the language and focus of the statute, [ii] its legislative history, and [iii] its purpose," is the primary basis for implication of a private right of action. 442 U.S. at 575-576, and thereby struck directly at the so-called "enforcement rationale" of *J. I. Case & Co. v. Borak*, 377 U.S. 426 (1964), upon which Mr. Gutter relies in his petition. This Court said:

> To the extent our analysis in today's decision differs from that of the Court in *Borak*, it suffices to say that in a series of cases since *Borak* we have adhered to a stricter standard for the implication of private causes of action, and we follow that standard today. *Cannon v. University of Chicago*, [441 U.S. 677 at 688-709]. The ultimate question is one of congressional intent, not one of whether the Court thinks that it can improve upon the statutory scheme that Congress enacted into law.
>
> [442 U.S. 560 at 578.]

Based upon this "stricter standard" for implementation of private rights of action, the Court of Appeals below, as well as the Court of Appeals for the Fourth Circuit in *Stern v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 603 F.2d 1073 (4th Cir. 1979), and the Court of Appeals for the Tenth Circuit in *Utah State University v. Bear, Stearns*

& Co., 549 F.2d 164 (10th Cir. 1977), *cert. den.*, 434 U.S. 890 (1977), have now repudiated the pre-*Cort v. Ash*, decisions in *Pearlstein I* and its progeny for two compelling reasons. First, both the statutory language and the legislative history of § 7 of the 1934 Act and its amendments are utterly silent as to any Congressional intent to create a private remedy for violations of the regulations promulgated under that section. Second, the legislative history makes it clear that investors were not intended to be the especial beneficiaries of § 7 of the 1934 Act. Moreover, this failure to satisfy the "threshold question" of especial benefit was reinforced by the enactment in 1970 of § 7(f) of the 1934 Act, 15 U.S.C. § 78g(f), which, for the first time, made investors as well as brokers and bankers responsible for extensions of credit in violation of the regulations promulgated under § 7 of the 1934 Act. As the Court of Appeals for the Sixth Circuit recently held in *Gilman v. Federal Deposit Insurance Corporation*, 660 F.2d 688 (6th Cir. 1981), a case which both followed and reaffirmed the decision below:

> [the enactment of] . . . section 7(f) remove[d] any lingering doubts about Congress' intention 'to confer federal rights' on borrowers. *California v. Sierra Club* . . . The fact that borrowers themselves are now regulated proves to us that section 7 was not enacted for their 'especial benefit.' *Piper v. Chris-Craft Inc.*, . . . ; *Gutter v. Merrill Lynch* . . .
>
> [660 F.2d 688 at 693.]

In short, the implication of a private right of action under § 7 of the 1934 Act is simply inconsistent with the "stricter standard" established by this Court.

Although no other Courts of Appeals have, as yet, had an opportunity to decide the question in the light of this Court's decision in *Cort v. Ash*, four Appellate Courts have raised and then side-stepped the question of the continuing validity of a private remedy after the enact-

ment of § 7(f) and this Court's decision in *Cort v. Ash.* The Seventh Circuit, in *Capos v. Mid-American National Bank of Chicago,* 581 F.2d 676 (7th Cir. 1978) noted that, although the parties had not briefed the issue, *Cort v. Ash,* seemed to cast doubt on the existence of a private cause of action. However, the court found it unnecessary to decide this issue since it sustained the lower court's holding that the claim, if it existed at all, was time barred. Two lower courts in the Seventh Circuit have, however, refused to imply a private cause of action, *Tucker v. Janota,* [1979] Fed. Sec. L. Rep. (CCH) ¶ 96,701 (N.D. Ill. November 1, 1978), and *Bassler v. Central National Bank in Chicago,* No. 81C-996 (N.D. Ill. June 9, 1981). Similarly, the Ninth Circuit in *Wyshak v. City National Bank,* 607 F.2d 824 (9th Cir. 1979) expressly reserved the question when it sustained the lower court's holding that any claim would be time barred, but a lower court in the Ninth Circuit has recently denied a private remedy under § 7 of the 1934 Act. *Furer v. Paine, Webber, Jackson & Curtis, Inc.,* [1981] Fed. Sec. L. Rep. (CCH) ¶ 98,367 (C.D. Cal. November 24, 1981). In *Shull v. Dain, Kalman & Quail, Inc.,* 561 F.2d 152 (8th Cir. 1977), *cert. den.,* 434 U.S. 1086 (1978), the Eighth Circuit also avoided consideration of the private cause of action issue when it sustained the lower court's finding that the defendant did not violate the margin regulations. Finally, the Fifth Circuit, in *McNeal v. Paine, Webber, Jackson & Curtis, Inc.,* 598 F.2d 888 (5th Cir. 1979), expressly declined to rule on the issue of a private cause of action under § 7 of the 1934 Act when it reversed the lower court's dismissal of the plaintiff's claims under § 10b and § 7 of the 1934 Act on the basis of the statute of limitations. The Fifth Circuit again refused to rule on the question in *Vigman v. Community National Bank & Trust Co.,* 635 F.2d 455 (5th Cir. 1981), where it upheld the lower court's summary judgment denying the claim as barred by the applicable Florida

statute of limitations. Three lower courts in the Fifth Circuit have since reached the issue and all have held that there is no implied private remedy. *Marrero v. Banco di Roma*, 487 F. Supp. 568 (E.D. La. 1980), *Martin v. Howard, Weil, Labouisse, Friedricks, Inc.*, 487 F. Supp. 503 (E.D. La. 1980), and *First Alabama Bancshares, Inc. v. Lowder*, [1981] Fed. Sec. L. Rep. (CCH) ¶ 98,015 (N.D. Ala. May 1, 1981).

Although the Second Circuit, which decided the leading case *Pearlstein I*, has never had the opportunity to reconsider its ruling in light of *Cort v. Ash*, when that case came before the Second Circuit for a second time on the issue of damages, that court prophetically warned that, "The effect of . . . [the intervening enactment of § 7(f) of the 1934 Act] is to cast doubt on the continuing viability of [*Pearlstein I*]." *Pearlstein v. Scudder & German*, 527 F.2d 1141 at 1145 n. 3 (2d Cir. 1975). At least seven lower courts in the Second Circuit have since heeded that warning and rejected a private cause of action under the margin regulations. *Drasner v. Thomson McKinnon Securities, Inc.*, 433 F. Supp. 485 (S.D.N.Y. 1977), *Schy v. F.D.I.C.*, 465 F. Supp. 766 (E.D.N.Y. 1977), *Theoharous v. Bache & Co.*, [1977-1978] Fed. Sec. L. Rep. (CCH) ¶ 96,281 (D. Conn. September 7, 1977), *Gluck v. Frankel*, 440 F. Supp. 1143 (S.D.N.Y. 1977), *Nussbacher v. Chase Manhattan Bank*, 444 F. Supp. 973 (S.D.N.Y. 1977), *Establissement Tomis v. Shearson Hayden Stone, Inc.*, 459 F. Supp. 1355 (S.D.N.Y. 1978), and *Siedman v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 465 F. Supp. 1233 (S.D.N.Y. 1979). Only three lower court decisions in the Second Circuit swim against this tide. *Palmer v. Thomson & McKinnon Auchincloss, Inc.*, 427 F. Supp. 915 (D. Conn. 1977), *Panayotopulas v. Chemical Bank*, 464 F. Supp. 199 (S.D.N.Y. 1979), and *Altschul v. Paine, Webber, Jackson & Curtis, Inc.*, 518 F. Supp. 591 (S.D.N.Y. 1981). However, all of these cases were decided prior to the Supreme Court's more recent decisions on implication of

private rights of action beginning with *Cannon v. University of Chicago*, and *Touche Ross & Co. v. Redington*, which have, in effect, refocused the inquiry under the *Cort v. Ash*, tests to whether or not Congress intended to create a private remedy.

2. Remedy Under § 12(2) and § 17(a) of the 1933 Act

The petition does not even attempt to advance any reasons why this Court should review the question of whether a seller of option contracts is entitled to relief against his broker either under § 12(2) or § 17(a) of the 1933 Act. In fact, Mr. Gutter appears to have conceded that the Court of Appeals correctly denied relief under § 12(2) and is only requesting this Court to consider whether a seller has an implied private right of action against his broker under § 17(a) of the 1933 Act.

The question presented is neither significant nor controversial. The Court of Appeals quite simply held that (i) the express statutory language of § 12(2) of the 1933 Act provides a remedy only for purchasers of securities against the persons from whom they purchased and (ii) under the language of § 17(a) of the 1933 Act an implied private right of action must be limited to relief against persons who offer or sell securities. Since Mr. Gutter, as a seller of uncovered options contracts, sold securities through the Chicago Board Options Exchange and did not purchase any securities from Merrill Lynch, the Court of Appeals readily concluded that Mr. Gutter could not possibly have sustained a claim under either § 12(2) or § 17(a) of the 1933 Act.

Mr. Gutter has not suggested that this decision is in conflict with any other appellate decision, nor has he challenged the Court of Appeals' determination that he was a seller and not a purchaser of securities. His sole argument seems to be that the decision of the Court of

Appeals is inconsistent with this Court's decision in *United States v. Naftalin*, 441 U.S. 768 (1979). However, Mr. Gutter's reliance upon this case is wholly inapposite. *Naftalin* was a criminal enforcement action against an investor who engaged in a short selling scheme which defrauded his brokers. Therefore, even if it is assumed that short selling and selling uncovered options are essentially equivalent transactions, *Naftalin* involves a situation which is virtually the mirror image of the instant case and in no way suggests that § 17(a) of the 1933 Act affords an implied private cause of action in favor of sellers of securities against their brokers.

CONCLUSION

For the reasons set forth above, Merrill Lynch respectfully submits that Mr. Gutter has failed to advance sufficient reasons why this Court should review either of the questions presented. Therefore, the petition should be denied.

Respectfully submitted,

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